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No. 77-597

In the Supreme Court of the United States

OCTOBER TERM, 1977

EPH H. HOOVER, JR. AND LUCINDA HOOVER, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

PETITIONERS' REPLY TO MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

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Pursuant to rule number 24(4) of the *Rules of the Supreme Court of the United States,* Petitioners hereby file this reply to the United States of America's Memorandum in Opposition to the Petition for a Writ of Certiorari to the United States Court of Appeals for the Sixth Circuit. In its memorandum in opposition, the Respondent is making the exact misapplication of *United States* v. *Generes,* 405 U.S. 93 (1972) that the Petitioners contend the lower Courts have made. Respondent, while making this misapplication of *Generes,* ignores other evidence that was available to the jury when it decided that

the Petitioner was entitled to a verdict. On page three (3) of its brief, the Respondent states:

> . . . the numerical comparison . . . is precisely what the Court in *Generes* held to be dispositive . . .

Thus it is readily apparent that the United States misapplies *Generes* as the lower courts did and holds that the numerical comparison is dispositive despite not only the existence of controverted financial evidence, but is also dispositive despite other evidence showing the taxpayer's dominant motivation.

The Petitioner contends that the financial analysis is not unfavorable to the taxpayer as the government contends in footnote two on page three of its memorandum in opposition. The government is assuming incorrectly that the Petitioners agree with the District Court's financial analysis. This is not correct. This is the precise reason why the Petitioners contend that the lower courts have ignored this Court's instructions as set forth in *Brady* v. *Southern Railroad,* 320 U.S. 476 (1943). While the District Court relies on the unrealized value of the taxpayer's investment in 1965 and 1966, the taxpayer contends that his original investment in all three companies was only $11,350. His salaries from the three companies were $19,000 in 1963 and $22,580 in 1964. Thus, it should be abundantly clear that the jury could have found, as it evidently did, that the guarantee was being made to protect the taxpayer's salary, not his original investment. Moreover, it would be inconceivable that a rational man would consider protecting an investment of $11,350 by personally signing guarantees for $800,000. Guarantees which he eventually had to make good in the amount of $549,000.

Not only is the government's memorandum ignoring the fact that the financial analysis was hotly disputed, but it also ignores the fact that also the original indemnification agreement was signed on October 2, 1963 and the second one was signed in July of 1964 for an additional $200,000

for a total of $800,000 of personal guarantees. The District Court considered the unrealized value of the Petitioner's investment during subsequent years to determine the taxpayer's dominant motivation on the dates the agreements were executed. Even if the District Court and the government were correct in considering the unrealized value of the Petitioner's investment, the proper date is the date the agreements were signed. The only evidence of Hoover, Inc.'s value would be its earned surplus of $223,936.20 for 1963 and $432,553.57 for 1964.* Hot-Mix, Inc. and its related companies which included John L. Burns had a negative earned surplus of $76,098.18 in 1964. Therefore, even if the Petitioner's unrealized gain, as reflected by the earned surplus, is a proper measure of value, it was certainly reasonable for the jury to determine that the taxpayer's dominant motive in signing the $800,000 guarantee was to protect his present and future salary. It is obvious that the jury could have reasonably believed that the taxpayer would not risk $800,000 to protect an investment that had an unrealized value of approximately $220,000 to $360,000 based solely on earned surplus.

The Jury could have reasonably found from the evidence, as its verdict indicates, that the Petitioner's dominant motivation in guaranteeing the loans was to retain and enhance his salary. One evidentiary basis for the jury decision's could be the Petitioner's evidence that

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*Of course, a corporation's earned surplus does not necessarily represent its fair market value. The earned surplus is merely the total earnings and profits retained and reinvested in the business. Most of the earned surplus could be represented by depreciated machinery and working capital necessary to finance the next construction job. In fact, due to the accounting profession's use of historical cost on balance sheets, it is highly unlikely that a corporation's earned surplus would represent its net liquidation value.

there are very few sales of construction companies. Thus, in addition to the other favorable evidence, there is more than sufficient evidence in the record to support the jury conclusion that the Petitioner was protecting and enhancing his employment rather than his equity investment in a corporation which he has very little chance of selling.

It was the jury's decision to determine the Petitioner's dominant motivation based on the financial information it believed was significant. By its verdict, it is obvious that the jury decided that the Petitioner's dominant motivation in advancing the $800,000 was to protect his salary and not a lesser investment. It was the jury's duty to determine the Petitioner's dominant motivation based on the evidence and not the Trial Court's duty to second guess the jury by granting a motion for judgment n.o.v., when the evidence is clearly conflicting. *Brady* v. *Southern Railroad, supra.*

The United States is also incorrect when it states that the District and Circuit Courts rules in *Anderson* v. *United States,* 555 F.2d 236 (C.A.9, 1977), that the objective economic evidence could not support a finding that the dominant motivation of a taxpayer was to protect his corporate investment rather than his employment. As noted in the Ninth Circuit opinion, the government relied on the objective economic evidence heavily to support its contention that the taxpayer's dominant motive was to protect his investment rather than his job. However, as a Ninth Circuit pointed out in *Anderson,* that evidence, the objective economic evidence, is not the only basis upon which the taxpayer's dominant motive could be determined. However, in its Memorandum in Opposition, the Respondent is now contending that the numerical comparison was held to be dispositive by this Court in *Generes.* If that is true, then the Court of Appeals for the Ninth Circuit is misapplying *Generes* and there is a conflict between it and the Sixth Circuit's opinion in this case. So, not only is the United States misconstruing

Generes and *Anderson,* but is ignoring this Court's dictates in *Brady* v. *Southern Railroad,* to determine the taxpayer's motivation in advancing money to John L. Burns, Inc.

Not only is the United States and the District Court relying on conflicting economic evidence, it is ignoring all the other objective factors which indicate that the Petitioner signed the guarantee for the dominant motivation of protecting his salary not his investment. The lower courts have ignored completely the evidence that the appellant had only one job, a job working for a corporation created to provide him with salaried employment. As opposed to the situation in *Generes,* the appellant did not create these corporations to provide his relatives with jobs. The evidence at trial established that the appellant worked long and hard hours for the corporation. He was not a passive officer and investor as was the situation in *Generes.* The present case is factually distinguishable by *Generes* in every manner. Moreover, contrary to the District Court's finding that the taxpayer has average income of $131,009.69 per year, his income tax returns for 1963 and 1964 showed additional income of $25,365.48 for 1963 and $38,439.05 for 1964. Moreover, it should be recognized that this additional income was from rent, royalties and pensions, etc. and did not constitute income from active employment. They were a passive source of income.

Thus, not only did the lower courts ignore the fact that the so-called objective economic evidence was in dispute as to the proper year and amounts, but they ignored other credible evidence that could have supported the jury's verdict in the taxpayer's favor. After the jury returned its favorable verdict for the taxpayer, the District Court weighted the evidence and decided that a different result was required. Thus, ignoring *Brady* v. *Southern Railroad,* the District Court took the jury verdict away from the

taxpayer by weighing the evidence and determining the facts contrary to the jury. Upon appeal, the Sixth Circuit Court of Appeals affirmed the District Court. Thus, it completely disregarded the dictates of *Brady* v. *Southern Railroad, supra.*

CONCLUSION

For the reasons stated, it is respectfully requested that the petition for a Writ of Certiorari should be granted.

Respectfully submitted,
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